

Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See 86 Ill. Adm. Code 130.220. (This is a PLR).

July 26, 2001

Dear Xxxxx:

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200 (see <http://www.revenue.state.il.us/legalinformation/regs/part1200>), is in response to your letter of May 7, 2001 and subsequent phone conversation. Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to AAA for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither AAA nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

In your letter, you have stated and made inquiry as follows:

As per our prior correspondence, we are writing to obtain a binding Private Letter Ruling regarding the sales taxes paid on the purchase of our equipment (see attached letters of our correspondence). We are not under audit, and yes the equipment was never located or used in Illinois. I am also enclosing the original lease. We purchased the equipment from BBB located in CITY/STATE, and we paid \$1,348.32 STATE State sales taxes. The equipment was shipped from CITY to our shop in CITY/STATE2. We financed the equipment originally through CCC, in CITY, Illinois. The original payment on the lease was to be \$599.89. After we made our first payment, they increased our monthly payment to \$658.42 to include Illinois state sales tax. We made 33 payments of \$658.42, which is a total of \$1,931.49 in Illinois state sales taxes. We brought it to their attention and they ignored us. We refinanced the equipment, through DDD in CITY2, Illinois, in 11/96 and again we brought it to their attention, but they ignored us. And, again our payments were originally \$340.00 per month. After making 5 payments, they then increased our monthly payment to \$365.00, to include Illinois sales tax. We have now made 38 payments of \$365.00, totaling \$950.00 in Illinois state sales tax. So, overall, we have paid \$1,359.88 in STATE state sales tax, and \$2,881.49 in Illinois state sales tax. We feel that we should never have been charged the Illinois state sales taxes for these reasons:

1. We paid STATE state sales taxes on the equipment when we bought it.
2. The equipment was never in Illinois. The transaction took place in STATE, and the equipment stayed in STATE.

As per your section 1200.110, Private letter rulings, enclosed you will find copies of:

1. The original lease documents.
2. The refinance lease documents.
3. The receipt from BBB for the equipment.
4. History of payments made on the equipment.
5. The original check sent to BBB from CCC.
6. The letter you sent to me concerning this issue.
7. My original letter to you concerning this issue.

References:

NAMES/ADDRESSES

If you need further information, or have any questions please feel free to call me at the above phone number. Thank you for your time and consideration on this matter.

As stated in the General Information letter sent to you on May 1, 2001, the State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases.

A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if lessors are guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction, thus making all receipts subject to Retailers' Occupation Tax.

A true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See the enclosed copy of 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. The State of Illinois imposes no tax on rental receipts. Consequently, lessees incur no tax liability.

The above guidelines are applicable to all true leases of tangible personal property in Illinois except for automobiles leased under terms of one year or less, which are subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq.

As stated above, in the case of a true lease, the lessors of the property being used in Illinois would be the parties with Use Tax obligations. The lessors would either pay their suppliers, if their suppliers were registered to collect Use Tax, or would self-assess and remit the tax to the Department. If the lessors already paid taxes in another state with respect to the acquisition of the tangible personal property, they would be exempt from Use Tax to the extent of the amount of such tax properly due and paid in such other state. See 86 Ill. Adm. Code 150.310(a)(3) enclosed.

Under Illinois law, lessors may not "pass through" their tax obligation on to the lessees as taxes. However, lessors and lessees may make private contractual arrangements for a reimbursement of the tax to be paid by the lessees. If lessors and lessees have made private agreements where lessees agree to reimburse lessors for the amount of the tax paid, then lessees are obligated to fulfill the terms of the private contractual agreements.

In regards to sale/leaseback situations, typically customer A purchases equipment from retailer B, and then sells it to lessor C who leases the equipment back to customer A. Customer A has paid tax when purchasing the equipment in the first transaction under a taxable retail sale and the second transaction (customer A's sale to lessor C) is a nontaxable occasional sale so long as A is not otherwise in the business of selling like-kind property. The third transaction (the leaseback of the equipment from lessor C to customer A) is not taxable because, as noted above, Illinois does not impose a sales/use tax on rental receipts with the exception of automobiles rented for a period of one year or less.

In general, no special documentation is required for any of the sale/leaseback transactions. In transaction 1 (sale from retailer B to customer A), retailer B would include the gross proceeds from its sale to customer A on its monthly sales tax returns and customer A would retain an invoice showing it paid tax to retailer B. In transaction 2 (sale from customer A to lessor C), it may be wise to document, on the invoice to lessor C, the fact that customer A is not otherwise in the business of selling like-kind equipment and that the sale is a nontaxable occasional sale. Transaction 3 (leaseback from lessor C to customer A) requires no documentation because rental receipts under true leases are not subject to Illinois sales tax liability (again, except automobiles rented for one year or less). The sale/leaseback transaction is not generally used with a conditional sale because there is no statutory mechanism to provide a credit for tax customer A properly paid in its previous purchase from B. If a sale/leaseback is used in conjunction with a conditional sale, tax will be due when lessor C conditionally sells the equipment back to A. To avoid this result A would need to lease the equipment from C under a true lease rather than a conditional sale.

The 1993 lease attached to your letter was a conditional sale. Sales tax liability was not incurred since the property was never located or used in Illinois. The 1997 lease is a true lease. However, as with the 1993 lease, the property has never been located or used in Illinois. Consequently, neither a sale nor a use (lease) of tangible personal property ever took place in Illinois. This being the case, no Illinois tax was ever due.

If a taxpayer pays an amount of tax under the Retailers' Occupation Tax Act that is not due, either as a result of a mistake of fact or an error of law, the taxpayer may file a claim for credit with the Department. Only the persons remitting tax to the Department are authorized to file such claims. No credit shall be given the taxpayer unless the taxpayer shows that it has borne the burden of the tax or has unconditionally repaid the amount of the tax to the customer from whom it was collected. See the enclosed copy of 86 Ill. Adm. Code 130.1501. The claims for credit must be prepared and filed upon forms provided by the Department containing the information listed in Section 130.1501(b).

Under Illinois sales tax laws, retailers are not required to file claims for credit. Further, the Department has no authority to compel sellers to file a claim for credit. Whether or not sellers refund the taxes paid and file claims for credit with the Department is a private matter between sellers and purchasers.

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

I hope this information is helpful. If you have further questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois

sales tax laws, please visit our website at www.revenue.state.il.us or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.